Republic of the Philippines
SUPREME COURT
Manila

EN BANC

G.R. No. L-4811 July 31, 1953

CHARLES F. WOODHOUSE, plaintiff-appellant,
vs.
FORTUNATO F. HALILI, defendant-appellant.

Tañada, Pelaez & Teehankee for defendant and appellant.
Gibbs, Gibbs, Chuidian & Quasha for plaintiff and appellant.

LABRADOR, *J.*:

On November 29, 1947, the plaintiff entered on a written agreement, Exhibit A, with the defendant, the most important provisions of which are (1) that they shall organize a partnership for the bottling and distribution of Mision soft drinks, plaintiff to act as industrial partner or manager, and the defendant as a capitalist, furnishing the capital necessary therefor; (2) that the defendant was to decide matters of general policy regarding the business, while the plaintiff was to attend to the operation and development of the bottling plant; (3) that the plaintiff was to secure the Mission Soft Drinks franchise for and in behalf of the proposed partnership; and (4) that the plaintiff was to receive 30 per cent of the net profits of the business. The above agreement was arrived at after various conferences and consultations by and between them, with the assistance of their respective attorneys. Prior to entering into this agreement, plaintiff had informed the Mission Dry Corporation of Los Angeles, California, U.S.A., manufacturers of the bases and ingridients of the beverages bearing its name, that he had interested a prominent financier (defendant herein) in the business, who was willing to invest half a million dollars in the bottling and distribution of the said beverages, and requested, in order that he may close the deal with him, that the right to bottle and distribute be granted him for a limited time under the condition that it will finally be transferred to the corporation (Exhibit H). Pursuant for this request, plaintiff was given "a thirty-days" option on exclusive bottling and distribution rights for the Philippines" (Exhibit J). Formal negotiations between plaintiff and defendant began at a meeting on November 27, 1947, at the Manila Hotel, with their lawyers attending. Before this meeting plaintiff's lawyer had prepared the draft of the agreement, Exhibit II or OO, but this was not satisfactory because a partnership, instead of a corporation, was desired. Defendant's lawyer prepared after the meeting his own draft, Exhibit HH. This last draft appears to be the main basis of the agreement, Exhibit A.

The contract was finally signed by plaintiff on December 3, 1947. Plaintiff did not like to go to the United States without the agreement being not first signed. On that day plaintiff and defendant went to the United States, and on December 10, 1947, a franchise agreement (Exhibit V) was entered into the Mission Dry Corporation and Fortunato F. Halili and/or Charles F. Woodhouse, granted defendant the exclusive right, license, and authority to produce, bottle, distribute, and sell Mision beverages in the Philippines. The plaintiff and the defendant thereafter returned to the Philippines. Plaintiff reported for duty in January, 1948, but operations were not begun until the first week of February, 1948. In January plaintiff was given as advance, on account of profits, the sum of P2,000, besides the use of a car; in February, 1948, also P2,000, and in March only P1,000. The car was withdrawn from plaintiff on March 9, 1948.

When the bottling plant was already on operation, plaintiff demanded of defendant that the partnership papers be executed. At first defendant executed himself, saying there was no hurry. Then he promised to do so after the sales of the product had been increased to P50,000. As nothing definite was forthcoming, after this condition was attained, and as defendant refused to give further allowances to plaintiff, the latter caused his attorneys to take up the matter with the defendant with a view to a possible settlement. as none could be arrived at, the present action was instituted.

In his complaint plaintiff asks for the execution of the contract of partnership, an accounting of the profits, and a share thereof of 30 per cent, as well as damages in the amount of P200,000. In his answer defendant alleges by way of defense (1) that defendant's consent to the agreement, Exhibit A, was secured by the representation of plaintiff that he was the owner, or was about to become owner of an exclusive bottling franchise, which representation was false, and plaintiff did not secure the franchise, but was given to defendant himself; (2) that

defendant did not fail to carry out his undertakings, but that it was plaintiff who failed; (3) that plaintiff agreed to contribute the exclusive franchise to the partnership, but plaintiff failed to do so. He also presented a counter-claim for P200,000 as damages. On these issues the parties went to trial, and thereafter the Court of First Instance rendered judgment ordering defendant to render an accounting of the profits of the bottling and distribution business, subject of the action, and to pay plaintiff 15 percent thereof. it held that the execution of the contract of partnership could not be enforced upon the parties, but it also held that the defense of fraud was not proved. Against this judgment both parties have appealed.

The most important question of fact to be determined is whether defendant had falsely represented that he had an exclusive franchise to bottle Mission beverages, and whether this false representation or fraud, if it existed, annuls the agreement to form the partnership. The trial court found that it is improbable that defendant was never shown the letter, Exhibit J, granting plaintiff had; that the drafts of the contract prior to the final one can not be considered for the purpose of determining the issue, as they are presumed to have been already integrated into the final agreement; that fraud is never presumed and must be proved; that the parties were represented by attorneys, and that if any party thereto got the worse part of the bargain, this fact alone would not invalidate the agreement. On this appeal the defendant, as appellant, insists that plaintiff did represent to the defendant that he had an exclusive franchise, when as a matter of fact, at the time of its execution, he no longer had it as the same had expired, and that, therefore, the consent of the defendant to the contract was vitiated by fraud and it is, consequently, null and void.

Our study of the record and a consideration of all the surrounding circumstances lead us to believe that defendant's contention is not without merit. Plaintiff's attorney, Mr. Laurea, testified that Woodhouse presented himself as being the exclusive grantee of a franchise, thus:

> A. I don't recall any discussion about that matter. I took along with me the file of the office with regards to this matter. I notice from the first draft of the document which I prepared which calls for the organization of a corporation, that the manager, that is, Mr. Woodhouse, is represented as being the exclusive grantee of a franchise from the Mission Dry Corporation. . . . (t.s.n., p.518)

As a matter of fact, the first draft that Mr. Laurea prepared, which was made before the Manila Hotel conference on November 27th, expressly states that plaintiff had the exclusive franchise. Thus, the first paragraph states:

> *Whereas, the manager is the exclusive grantee of a franchise from the Mission Dry Corporation San Francisco, California*, for the bottling of Mission products and their sale to the public throughout the Philippines; . . . .
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> 3. The manager, upon the organization of the said corporation, shall forthwith transfer to the said corporation his exclusive right to bottle Mission products and to sell them throughout the Philippines. . . . .
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> (Exhibit II; emphasis ours)

The trial court did not consider this draft on the principle of integration of jural acts. We find that the principle invoked is inapplicable, since the purpose of considering the prior draft is not to vary, alter, or modify the agreement, but to discover the intent of the parties thereto and the circumstances surrounding the execution of the contract. The issue of fact is: Did plaintiff represent to defendant that he had an exclusive franchise? Certainly, his acts or statements prior to the agreement are essential and relevant to the determination of said issue. The act or statement of the plaintiff was not sought to be introduced to change or alter the terms of the agreement, but to prove how he induced the defendant to enter into it — to prove the representations or inducements, or fraud, with which or by which he secured the other party's consent thereto. These are expressly excluded from the parol evidence rule. (Bough and Bough vs. Cantiveros and Hanopol, 40 Phil., 209; port Banga Lumber Co. *vs*. Export & Import Lumber Co., 26 Phil., 602; III Moran 221,1952 rev. ed.) Fraud and false representation are an incident to the creation of a jural act, not to its integration, and are not governed by the rules on integration. Were parties prohibited from proving said representations or inducements, on the ground that the agreement had already been entered into, it would be impossible to prove misrepresentation or fraud. Furthermore, the parol evidence rule expressly allows the evidence to be introduced when the validity of an instrument is put in issue by the pleadings (section 22, par. (a), Rule 123, Rules of Court),as in this case.

That plaintiff did make the representation can also be easily gleaned from his own letters and his own testimony. In his letter to Mission Dry Corporation, Exhibit H, he said:.

> . . . He told me to come back to him when I was able to speak with authority so that we could come to terms as far as he and I were concerned. That is the reason why the cable was sent. Without this authority, I am in a poor bargaining position. . .
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> I would propose that you grant me the exclusive bottling and distributing rights for a limited period of time, during which I may consummate my plants. . . .

By virtue of this letter the option on exclusive bottling was given to the plaintiff on October 14, 1947. (See Exhibit J.) If this option for an exclusive franchise was intended by plaintiff as an instrument with which to bargain with defendant and close the deal with him, he must have used his said option for the above-indicated purpose, especially as it appears that he was able to secure, through its use, what he wanted.

Plaintiff's own version of the preliminary conversation he had with defendant is to the effect that when plaintiff called on the latter, the latter answered, "Well, come back to me when you have the authority to operate. I am definitely interested in the bottling business." (t. s. n., pp. 60-61.) When after the elections of 1949 plaintiff went to see the defendant (and at that time he had already the option), he must have exultantly told defendant that he had the authority already. It is improbable and incredible for him to have disclosed the fact that he had *only an option* to the exclusive franchise, which was to last thirty days only, and still more improbable for him to have disclosed that, at the time of the signing of the formal agreement, *his option had already expired*. Had he done so, he would have destroyed all his bargaining power and authority, and in all probability lost the deal itself.

The trial court reasoned, and the plaintiff on this appeal argues, that plaintiff only undertook in the agreement "to secure the Mission Dry franchise for and in behalf of the proposed partnership." The existence of this provision in the final agreement does not militate against plaintiff having represented that he had the exclusive franchise; it rather strengthens belief that he did actually make the representation. How could plaintiff assure defendant that he would get the franchise for the latter if he had not actually obtained it for himself? Defendant would not have gone into the business unless the franchise was raised in his name, or at least in the name of the partnership. Plaintiff assured defendant he could get the franchise. Thus, in the draft prepared by defendant's attorney, Exhibit HH, the above provision is inserted, with the difference that instead of securing the franchise for the defendant, plaintiff was to secure it for the partnership. To show that the insertion of the above provision does not eliminate the probability of plaintiff representing himself as the exclusive grantee of the franchise, the final agreement contains in its third paragraph the following:

> . . . and the manager is ready and willing to allow the capitalists to use the exclusive franchise . . .

and in paragraph 11 it also expressly states:

> 1. In the event of the dissolution or termination of the partnership, . . . the franchise from Mission Dry Corporation shall be reassigned to the *manager*.

These statements confirm the conclusion that defendant believed, or was made to believe, that plaintiff was the grantee of an exclusive franchise. Thus it is that it was also agreed upon that the franchise was to be transferred to the name of the partnership, and that, upon its dissolution or termination, the same shall be reassigned to the plaintiff.

Again, the immediate reaction of defendant, when in California he learned that plaintiff did not have the exclusive franchise, was to reduce, as he himself testified, plaintiff's participation in the net profits to one half of that agreed upon. He could not have had such a feeling had not plaintiff actually made him believe that he (plaintiff) was the exclusive grantee of the franchise.

The learned trial judge reasons in his decision that the assistance of counsel in the making of the contract made fraud improbable. Not necessarily, because the alleged representation took place before the conferences were had, in other words, plaintiff had already represented to defendant, and the latter had already believed in, the existence of plaintiff's exclusive franchise before the formal negotiations, and they were assisted by their lawyers only when said formal negotiations actually took place. Furthermore, plaintiff's attorney testified that plaintiff had said that he had the exclusive franchise; and defendant's lawyer testified that plaintiff explained to him, upon being asked for the franchise, that he had left the papers evidencing it.(t.s.n., p. 266.)

We conclude from all the foregoing that plaintiff did actually represent to defendant that he was the holder of the exclusive franchise. The defendant was made to believe, and he actually believed, that plaintiff had the exclusive franchise. Defendant would not perhaps have gone to California and incurred expenses for the trip, unless he believed that plaintiff did have that exclusive privilege, and that the latter would be able to get the same from the Mission Dry Corporation itself. Plaintiff knew what defendant believed about his (plaintiff's) exclusive franchise, as he induced him to that belief, and he may not be allowed to deny that defendant was induced by that belief. (IX Wigmore, sec. 2423; Sec. 65, Rule 123, Rules of Court.)

We now come to the legal aspect of the false representation. Does it amount to a fraud that would vitiate the contract? It must be noted that fraud is manifested in illimitable number of degrees or gradations, from the innocent praises of a salesman about the excellence of his wares to those malicious machinations and representations that the law punishes as a crime. In consequence, article 1270 of the Spanish Civil Code distinguishes two kinds of (civil) fraud, the causal fraud, which may be a ground for the annulment of a contract, and the incidental deceit, which only renders the party who employs it liable for damages. This Court had held that in order that fraud may vitiate consent, it must be the causal (*dolo causante*), not merely the incidental (*dolo causante*), inducement to the making of the contract. (Article 1270, Spanish Civil Code; Hill vs. Veloso, 31 Phil.

160.) The record abounds with circumstances indicative that the fact that the principal consideration, the main cause that induced defendant to enter into the partnership agreement with plaintiff, was the ability of plaintiff to get the exclusive franchise to bottle and distribute for the defendant or for the partnership. The original draft prepared by defendant's counsel was to the effect that plaintiff obligated himself to secure a franchise for the defendant. Correction appears in this same original draft, but the change is made not as to the said obligation but as to the grantee. In the corrected draft the word "capitalist"(grantee) is changed to "partnership." The contract in its final form retains the substituted term "partnership." The defendant was, therefore, led to the belief that plaintiff had the exclusive franchise, but that the same was to be secured for or transferred to the partnership. The plaintiff no longer had the exclusive franchise, or the option thereto, at the time the contract was perfected. But while he had already lost his option thereto (when the contract was entered into), the principal obligation that he assumed or undertook was to secure said franchise for the partnership, as the bottler and distributor for the Mission Dry Corporation. We declare, therefore, that if he was guilty of a false representation, this was not the causal consideration, or the principal inducement, that led plaintiff to enter into the partnership agreement.

But, on the other hand, this supposed ownership of an exclusive franchise was actually the consideration or price plaintiff gave in exchange for the share of 30 percent granted him in the net profits of the partnership business. Defendant agreed to give plaintiff 30 per cent share in the net profits because he was transferring his exclusive franchise to the partnership. Thus, in the draft prepared by plaintiff's lawyer, Exhibit II, the following provision exists:

> 3. That the MANAGER, upon the organization of the said corporation, shall forthwith *transfer* to the said corporation *his exclusive* right to bottle Mission products and to sell them throughout the Philippines. *As a consideration for such transfer, the CAPITALIST shall transfer to the Manager fully paid non assessable shares of* the said corporation . . . twenty-five per centum of the capital stock of the said corporation. (Par. 3, Exhibit II; emphasis ours.)

Plaintiff had never been a bottler or a chemist; he never had experience in the production or distribution of beverages. As a matter of fact, when the bottling plant being built, all that he suggested was about the toilet facilities for the laborers.

We conclude from the above that while the representation that plaintiff had the exclusive franchise did not vitiate defendant's consent to the contract, it was used by plaintiff to get from defendant a share of 30 per cent of the net profits; in other words, by pretending that he had the exclusive franchise and promising to transfer it to defendant, he obtained the consent of the latter to give him (plaintiff) a big slice in the net profits. This is the *dolo incidente* defined in article 1270 of the Spanish Civil Code, because it was used to get the other party's consent to a big share in the profits, an incidental matter in the agreement.

> El dolo incidental no es el que puede producirse en el cumplimiento del contrato sino que significa aqui, el que concurriendoen el consentimiento, o precediendolo, no influyo para arrancar porsi solo el consentimiento ni en la totalidad de la obligacion, sinoen algun extremo o accidente de esta, dando lugar tan solo a una accion para reclamar indemnizacion de perjuicios. (8 Manresa 602.)

Having arrived at the conclusion that the agreement may not be declared null and void, the question that next comes before us is, May the agreement be carried out or executed? We find no merit in the claim of plaintiff that the partnership was already a *fait accompli* from the time of the operation of the plant, as it is evident from the very language of the agreement that the parties intended that the execution of the agreement to form a partnership was to be carried out at a later date. They expressly agreed that *they shall form a partnership*. (Par. No. 1, Exhibit A.) As a matter of fact, from the time that the franchise from the Mission Dry Corporation was obtained in California, plaintiff himself had been demanding that defendant comply with the agreement. And plaintiff's present action seeks the enforcement of this agreement. Plaintiff's claim, therefore, is both inconsistent with their intention and incompatible with his own conduct and suit.

As the trial court correctly concluded, the defendant may not be compelled against his will to carry out the agreement nor execute the partnership papers. Under the Spanish Civil Code, the defendant has an obligation *to do*, not to give. The law recognizes the individual's freedom or liberty to do an act he has promised to do, or not to do it, as he pleases. It falls within what Spanish commentators call *a very personal* act (acto personalismo), of which courts may not compel compliance, as it is considered an act of violence to do so.

> *Efectos de las obligaciones consistentes en hechos personalismo*.—Tratamos de la ejecucion de las obligaciones de hacer en el solocaso de su incumplimiento por parte del deudor, ya sean los hechos personalisimos, ya se hallen en la facultad de un tercero; porque el complimiento espontaneo de las mismas esta regido por los preceptos relativos al pago, y en nada les afectan las disposiciones del art. 1.098.
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> Esto supuesto, la primera dificultad del asunto consiste en resolver si el deudor puede ser precisado a realizar el hecho y porque medios.

> Se tiene por corriente entre los autores, y se traslada generalmente sin observacion el principio romano *nemo potest precise cogi ad factum*. Nadie puede ser obligado violentamente a haceruna cosa. Los que perciben la posibilidad de la destruccion deeste principio, añaden que, aun cuando se pudiera obligar al deudor, no deberia hacerse, porque esto constituiria una violencia, y noes la violenciamodo propio de cumplir las obligaciones (Bigot, Rolland, etc.). El maestro Antonio Gomez opinaba lo mismo cuandodecia que obligar por la violencia seria infrigir la libertad eimponer una especie de esclavitud.
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> En efecto; las obligaciones contractuales no se acomodan biencon el empleo de la fuerza fisica, no ya precisamente porque seconstituya de este modo una especie de esclavitud, segun el dichode Antonio Gomez, sino porque se supone que el acreedor tuvo encuenta el caracter personalisimo del hecho ofrecido, y calculo sobre laposibilidad de que por alguna razon no se realizase. Repugna,ademas, a la conciencia social el empleo de la fuerza publica, mediante coaccion sobre las personas, en las relaciones puramente particulares; porque la evolucion de las ideas ha ido poniendo masde relieve cada dia el respeto a la personalidad humana, y nose admite bien la violencia sobre el individuo la cual tiene caracter visiblemente penal, sino por motivos que interesen a la colectividad de ciudadanos. Es, pues, posible y licita esta violencia cuando setrata de las obligaciones que hemos llamado *ex lege*, que afectanal orden social y a la entidad de Estado, y aparecen impuestas sinconsideracion a las conveniencias particulares, y sin que por estemotivo puedan tampoco ser modificadas; pero no debe serlo cuandola obligacion reviste un interes puramente particular, como sucedeen las contractuales, y cuando, por consecuencia, paraceria salirseel Estado de su esfera propia, entrado a dirimir, con apoyo dela fuerza colectiva, las diferencias producidas entre los ciudadanos. (19 Scaevola 428, 431-432.)

The last question for us to decide is that of damages,damages that plaintiff is entitled to receive because of defendant's refusal to form the partnership, and damages that defendant is also entitled to collect because of the falsity of plaintiff's representation. (Article 1101, Spanish Civil Code.) Under article 1106 of the Spanish Civil Code the measure of damages is the actual loss suffered and the profits reasonably expected to be received, embraced in the terms *daño emergente* and *lucro cesante*. Plaintiff is entitled under the terms of the agreement to 30 per cent of the net profits of the business. Against this amount of damages, we must set off the damage defendant suffered by plaintiff's misrepresentation that he had obtained a very high percentage of share in the profits. We can do no better than follow the appraisal that the parties themselves had adopted.

When defendant learned in Los Angeles that plaintiff did not have the exclusive franchise which he pretended he had and which he had agreed to transfer to the partnership, his spontaneous reaction was to reduce plaintiff's share form 30 per cent to 15 per cent only, to which reduction defendant appears to have readily given his assent. It was under this understanding, which amounts to a virtual modification of the contract, that the bottling plant was established and plaintiff worked as Manager for the first three months. If the contract may not be considered modified as to plaintiff's share in the profits, by the decision of defendant to reduce the same to one-half and the assent thereto of plaintiff, then we may consider the said amount as a fair estimate of the damages plaintiff is entitled to under the principle enunciated in the case of *Varadero de Manila vs. Insular Lumber Co*., 46 Phil. 176. Defendant's decision to reduce plaintiff's share and plaintiff's consent thereto amount to an admission on the part of each of the reasonableness of this amount as plaintiff's share. This same amount was fixed by the trial court. The agreement contains the stipulation that upon the termination of the partnership, defendant was to convey the franchise back to plaintiff (Par. 11, Exhibit A). The judgment of the trial court does not fix the period within which these damages shall be paid to plaintiff. In view of paragraph 11 of Exhibit A, we declare that plaintiff's share of 15 per cent of the net profits shall continue to be paid while defendant uses the franchise from the Mission Dry Corporation.

With the modification above indicated, the judgment appealed from is hereby affirmed. Without costs.

Paras, C.J., Pablo, Bengzon, Tuason, Montemayor, Reyes, Jugo and Bautista Angelo, JJ., concur.